

## Memorandum 76-42

Subject: Study 77.50 - Nonprofit Corporations (Corporate Finances)

The existing General Nonprofit Corporation Law contains few provisions specifically regulating the finances of nonprofit corporations; the statutes relating to supervision by the Attorney General (Section 9505) and common trust funds (Sections 10250 and 10251, technically not a part of the General Nonprofit Corporation Law) are notable exceptions. Most provisions relating to finances consist of general authorizations to impose dues and assessments and regulate memberships (Sections 9301, 9402, 9403, 9608, 9611).

The extent of the application (through Section 9002) of the finance provisions of the General Corporation Law (chiefly Part 4, Sections 1100-1910, and Chapter 3 of Part 5, Sections 2700-2714) to nonprofit corporations has not been delineated by caselaw or other authorities. Because of the definition of shares of stock to include memberships (Section 115), it is reasonable to conclude that the General Corporation Law provisions relating to issuance of shares and liabilities in connection therewith, redemption authority and procedure, and assessment procedures apply to nonprofit corporations issuing memberships with associated proprietary rights, at least in the absence of the adoption of specific bylaws or articles in these areas. See 56 Ops. Atty. Gen. 317 (1973). In view of the nature of and legal limitations upon nonprofit corporations, it seems equally clear that the provisions relating to dividends, stated capital, and capital reduction are inapplicable.

The corporate finance provisions of the new General Corporation Law are contained in Chapters 4 (issuance of shares, redemption, convertible shares, options, pre-emptive rights, employee stock plans, consideration, subscription and transferee liability, share certificates, transfer agent, and assessments) and 5 (procedure and financial requirements for dividends and corporate acquisition of its own shares). These sections generally continue existing California statutes, with most changes intended simply to increase the clarity or flexibility of the former sections. The significant exception to this rule occurs in Section 500, in which new financial requirements for the payment of

dividends or the reacquisition of shares are imposed on corporations. This section substitutes for the prior general requirement (former Section 1500, 1706-1707) that such payments be made out of "earned surplus" a new rule that the corporation's financial statements must demonstrate its financial ability (by way of retained earnings or net worth and current liquidity) before making the payments. The changes made by the new General Corporation Law have been followed in preparing the attached staff draft of Chapter 5.

#### General Organization of Chapter 5

Article 1. General Provisions. The sections concerning dues and assessments have been taken from existing law or drafted in response to Commission request. The remaining sections relating to lost or destroyed certificates are adapted from the General Corporation Law.

Certain topics which are found in Chapters 4 and 5 of the new General Corporation Law and which might have been placed in this article (or in an additional article in this chapter) have been omitted. Because of their inapplicability to nonprofit corporations, provisions concerning employee stock purchase plans and stock transfer agent liability are missing. Also omitted are provisions regulating classes of stock, conversion rights, options, pre-emption rights, transfer of stock and associated liabilities, share fractions, and stock certificates; these items, where applicable to memberships or securities of nonprofit corporations, should be covered in Chapter 4 (Members) or Articles 2, 3, and 4 (Capital Contributions, Subventions, and Debt, respectively) of Chapter 5.

Articles 2 (Capital Contributions), 3 (Subventions), and 4 (Debt). The contents of these articles are entirely new to the law of California, except to the extent that general authorization to issue memberships, require assessments and incur debt has been granted to nonprofit corporations. The capital contribution and subvention concepts and the specific debt limitations are taken from the law of New York and Pennsylvania; the relevant statutes from those states are attached as Exhibits I and II to this memorandum.

Article 2 authorizes a nonprofit corporation to require members to make capital contributions which may be repaid to the members (without interest or appreciation) under certain circumstances; in effect,

this is a particular kind of assessment. Article 3 authorizes the issuance of subventions, a type of subordinated debt. A subvention may earn interest, be redeemable at the option of the corporation or the holder, be transferable, and be repaid (with interest) upon dissolution: the rights of a subvention holder are always subordinate to those of creditors of the corporation. Article 4 places certain restrictions upon the issuance and repayment of evidences of indebtedness.

Two somewhat conflicting purposes are ascribed to the New York statutes governing nonprofit corporation finance from which Articles 2, 3, and 4 are derived: the enhancement of financing opportunities for nonprofit corporations through authorization of such new devices as capital contributions and subventions, and the strict regulation of any such financing in order to prevent the misuse of the nonprofit corporate form. See N.Y. Not-for-Profit Corp. Law §§ 502, 504, 506 (McKinney 1970); Note, New York's New Not-for-Profit Corporation Law, 47 N.Y.U. L. Rev. 761, 783-784 (1972). The staff does not believe, as explained below, that these reasons justify the inclusion of such provisions in the California General Nonprofit Corporation Law. Nevertheless, in order to provide the Commission with a version of these financing provisions adapted to the scheme of the new Law, Articles 2, 3, and 4 are included in the staff draft of this Chapter.

The staff doubts that the explicit authorization of capital contributions and subventions will expand the financing capabilities of nonprofit corporations. These devices consist of specialized versions of membership assessments and debt instruments, both of which may presently be issued by California nonprofit corporations under the authority of Sections 9301, 9402, 9403, 9501(f), and 9611. This authority will be continued by Sections 5230, 5410, and 5500. The specific requirements contained in the capital contribution and subvention provisions would actually limit the range of financing devices directly, and these articles might also do so indirectly by implying that no other such specialized devices are authorized.

It is also doubtful whether California requires further regulation of the finances of its nonprofit corporations; at least, there is a paucity of existing case law or other authority indicating that either nonprofit corporation members or other citizens are being injured by the financial misdeeds of nonprofit corporations. Through their control

over the contents of the articles and bylaws, members can regulate the levies upon themselves. The public's interest in the proper use of the nonprofit form, particularly as respects the custody and utilization of charitable property, is protected both by the prohibition on the distribution of profits and the investigatory and regulatory power of the Attorney General.

Article 5. Redemption. Existing law contains no redemption procedures specifically for nonprofit corporations. This article is an adaptation of Section 509 of the General Corporation Law, a continuation of former Sections 1700-1703. If Articles 2, 3, and 4 are not approved, the language of this article should be changed to delete the references to capital contributions and subventions while some language covering "other securities" should be added.

Article 6. Payments to members. This article is an adaptation of Section 500 (Distributions to shareholders). The language of its provisions should also be changed if Articles 2, 3, and 4 are not approved.

Article 7. Trust Property. Collected in this article are provisions of the existing General Nonprofit Corporation Law, certain provisions regulating corporations for charitable or eleemosynary purposes (Sections 10200 et seq.), and existing case law, all concerned with the acquisition and management of property specifically held upon a charitable trust, donated for expressed charitable purposes, or received by a corporation organized for or conducting itself in furtherance of charitable purposes.

Article 8. Common Trust Fund. The sections in this article continue the provisions of existing Sections 10250 and 10251 which authorize nonprofit corporations with charitable purposes to form and invest in common trust funds and which authorize certain educational organizations to join nonprofit corporations for the purpose of participating in such funds. While these sections are not now in the General Nonprofit Corporation Law, their broad application to nonprofit corporations makes such placement in the new General Nonprofit Corporation Law desirable.

#### Discussion of Individual Sections

##### § 5500. Levy of dues and assessments

This section was tentatively approved as Section 5510 in February 1976.

§ 5501. Levy of assessments

At the February 1976 meeting, the Commission directed the staff to consider possible approaches to permitting members to avoid burdensome assessments, including the requirement of class approval for assessments or the right of withdrawal from membership. The staff draft utilizes the latter approach.

The right of withdrawal is conditioned upon the imposition of an assessment three times greater than regular annual dues or assessments. This requirement is intended to prevent a member from using the section to avoid payment of assessments in amounts bearing some reasonable relationship to the normal financial burdens of membership. It establishes for both corporate management and members a clear limit to the coercive financial power of the corporation.

The staff believes that this type of standard is preferable to a requirement that the assessment be for future liabilities because of the difficult fact questions and the opportunities for financial manipulation inherent in "future liabilities" language. Further, it is probable that assessments significantly greater than normal annual payments (whether in the form of dues or annual assessment) will in fact be for the purpose of incurring new liabilities rather than for current operating deficits; at a minimum, this should become the case as management learns that it may be difficult to cover large deficits with extraordinary assessments.

Subdivision (b) provides for notice of such assessments to be given to members. Without such notice, action by the nonprofit corporation giving rise to the right of withdrawal might not be known to members.

Existing statutes and case law do not provide any specific protection for members upon whom extraordinary financial burdens are imposed. Those states which have enacted legislation concerning the imposition of assessments by nonprofit corporations all have provisions similar to existing California law (Section 9301) simply authorizing the adoption of articles, bylaws, or board resolutions governing assessment amounts and procedures. Some states have enacted specific limitations on the imposition of fines and penalties. E.g., Conn. Gen. Stat. Ann. tit. 33, § 33-446 (1960)(limited to amount of annual dues or assessment, or initiation fee).

No California cases on this question were located. Existing decisions from other states uphold the right of a nonprofit corporation to collect an assessment from a member who attempts to escape liability by resignation. See Locust Club v. Einstein, 129 Pa. Super. 338, 195 A. 432 (1937)(and cases cited therein).

California cases involving other rights of members exhibit a certain ambivalence. On the one hand, the courts have adopted the theory that an implied contract based upon the articles and bylaws exists between member and corporation, binding the member in advance to abide by the rules of the corporation (including imposition of assessments). See DeMille v. American Fed. of Radio Artists, 31 Cal.2d 139, cert. denied, 333 U.S. 876 (1947)(expulsion from membership for failure to pay one dollar assessment upheld, although resulting in termination of employment with value of almost \$100,000 annually). In contrast, California decisions also guarantee certain "rudimentary rights" to members and seek to protect them from "unreasonable or arbitrary" acts by the corporation. See Cason v. Glass Bottle Blowers Assn., 37 Cal.2d 134 (1951)(expulsion from union); Haynes v. Annendale Golf Club, 4 Cal.2d 28 (1935)(acceptance of resignation from club); Taboada v. Sociedad Espanola, etc., 191 Cal. 187 (1923)(expulsion from mutual benefit society). Recent cases have emphasized both the increased concern of the courts for the rights of members of private organizations and the principle that the extent of judicial scrutiny of the treatment of members will vary according to the significance of the member's interests at stake and the nature of the organization involved. See Erickson v. Gospel Foundation of Calif., 43 Cal.2d 581, 585 (1954); Ascherman v. San Francisco Medical Society, 39 Cal. App.3d 623, 647-650 (1974).

Given these cases, it is quite possible that the courts would refuse to allow a corporation to collect an assessment not arising from past operations from a member who resigns upon learning of the assessment. Cf. Griffiths & Sprague Steve. Co. v. Waterfront Emp. Assn., 162 Fed.2d 1017 (9th C. 1947) (upholding right of nonprofit corporation to levy assessments upon nonvoting members under California law, with dictum implying that member's failure to resign might have been a factor in the decision). The proposed Section 5501 may thus be unnecessary.

The draft section does not attempt to deal with the future relationship between the nonprofit corporation and the withdrawing member; for instance, should the former member be allowed to rejoin later without paying the assessment? The Comment to the section points this out. In conformity with the general grant of authority to nonprofit corporations to regulate themselves, the staff believes that no attempt to provide specific solutions to such questions should be made.

Another possible approach to protecting members in the general area of assessments is the enactment of tight procedural rules for the entire assessment process. Such provisions are presently contained in Sections 2700 through 2714 and are continued in new Section 423; included are rules for notice of the levy of assessments, service and publication of notice, time periods for payment and delinquency, assessment lien upon shares, late payment penalties, notice of and procedures for sale of delinquent shares, and forfeiture of shares. Such provisions are not presently applicable to nonprofit corporations (Section 2700 limits the application of the chapter to "shares issued by stock corporations").

Such procedural regulation should not be extended to nonprofit corporations for two reasons. First, it is unlikely to be effective with regard to the problem of members burdened by assessments for future liabilities; no opportunities for withdrawal are given. Second, these detailed procedures are appropriate for stock corporations in which an assessment is an extraordinary occasion but not for nonprofit corporations for which assessments are a common and necessary method of financing.

#### § 5513. Capital certificates

The draft section follows the lead of Pennsylvania rather than that of New York in making the issuance of certificates optional and in allowing for transferability if the nonprofit corporation desires. Compare Pa. Stat. Ann. tit. 15, § 7541(c) and (d)(1972) with N.Y. Not-for-Profit Corp. Law § 502 (McKinney 1970). The staff sees no substantial reason to require certificates or to limit the transfer of certificates.

§ 5515. Officers' certificate

Neither the Pennsylvania nor New York statutes contain a section comparable to this although the effect of the New York requirement (Section 502) that authority for imposing capital contribution requirements be in the articles is the same. However, given the substantial financial burden which may be involved, it is reasonable that the authority for and terms of capital contribution requirements be of public record.

Note. If Section 5501 is approved to provide members with a procedure for avoiding burdensome assessments, consideration should be given to drafting a similar section relating to the imposition of capital contribution requirements.

§ 5523. Periodic payments

This section authorizes payment of interest upon subvention certificates. Like the Pennsylvania statute (Section 7542) but unlike that of New York (Section 504) no maximum rate is set forth. The maximum allowed by New York is two-thirds of the usury rate (which varies between six and eight percent).

The staff does not believe a maximum is necessary or appropriate. A nonprofit corporation is presently free to negotiate for financing within the constraints of the usury law and should continue to have this capability. There is no reason why a person who is willing to furnish money or other property to a nonprofit corporation subject to the prior rights of all other creditors should also have to accept minimal interest payments although he is free to agree to such a scheme with the nonprofit corporation. Finally, payment to holders of subvention certificates who are also members is limited by the strictures of Sections 5236, 5551, and 5552.

§ 5527. Transfer

As with capital certificates, the proposed section would allow transfer at the option of the nonprofit corporation. Both Pennsylvania (Section 7543(d)) and New York (Section 503(a)) allow the corporation to provide for transfer rights.

§ 5529. Officers' certificate

See discussion of Section 5515.

#### § 5530. Debt

The requirement of specific consideration for the issuance of evidences of indebtedness is new. Neither existing law nor the new General Corporation Law extend the specific requirement of particular types of consideration for the issuance of shares to the issuance of debt instruments (although the definition of shares (Section 184) as divisions of proprietary interest in the corporation would make such requirements applicable to debt instruments with equity features). The Pennsylvania (Section 7543) and New York (Section 506) statutes both specify acceptable consideration.

The two major types of consideration excluded from the terms of this section are future services and promissory notes of the issuee. The prohibition against issuance for future consideration of equity certificates evidencing present rights is understandable, but the need to guard against issuance of debt instruments containing rights maturing only in the future in exchange for the promise of future performance on the part of the issuee is not as clear.

#### § 5531. Interest

Existing California law places no limits upon the interest rate to be paid by a nonprofit corporation other than the usury prohibition and the general rule against distribution of profits. The Pennsylvania Corporation Not-for-profit Code is similar (Section 7543), as are the laws of most states. The exception is New York, which allows payment only of "reasonable" interest, premiums, and discounts, and further limits interest payments to debt holders who are also members to the higher of the usury rate (between six and eight percent) and one percent over the prime rate in the Federal Reserve District of New York. N.Y. Not-for-Profit Corp. Law, § 506 (McKinney 1970).

The draft section is based upon Section 506(b) of the New York law, with the deletion of the "reasonable" standard for interest, premiums, and discounts, and the deletion of the specific interest ceiling for members. In addition, the New York prohibition against receipt by any holder of income or profit of the nonprofit corporation has been modified to provide that no interest, premium, or discount shall be calculated or contingent upon such income or profit.

The staff does not believe that specific interest maximums are appropriate; a nonprofit corporation should not be hamstrung in its attempts to obtain financing. The general prohibition on distribution of profits and the specific requirement in this section that the rate of return on debt investment not be dependant upon corporate income or profits are sufficient safeguards against exploitation of the nonprofit corporation to the detriment of either its members or the public.

§ 5550. Payments to members

§ 5551. Requirements for payments

Existing law contains no specific prohibitions on payments to members of nonprofit corporations; the general prohibition on the distribution of gains or profits stands alone. By incorporation, however, the General Corporation Law limits on repurchase of shares (Sections 1706-1708) should apply to repurchase of memberships. These sections generally require that such payments be made from earned surplus.

Section 500 embodies new standards for payment of dividends and purchase or redemption of shares: the existence of retained earnings or a combination of net worth and current liquidity. With some language changes in order to conform to general accounting practices for nonprofit corporations, these provisions have been adopted for Sections 5550 and 5551. Since the general purpose of these provisions--the protection of creditors--is the same, the use of similar standards is also appropriate.

This section does not apply to the repayment of debt instruments held by members in conformity with existing law and the scheme of the new General Corporation Law. Both the Pennsylvania (Section 7553) and New York (Sections 506 and 515, as to interest) statutes place similar financial prerequisites upon payments to members holding evidences of indebtedness, as part of the general policy of guarding against exploitation by members.

§ 5562. Institutional trustee

Subdivision (c) requires the periodic payment of income by the trustee to the nonprofit corporation. This type of requirement is also found in Sections 5563, 5574, and 5575. The rule that prohibits accumu-

lation of income on charitable assets (for varying periods of time) appears regularly in state statutes and the Internal Revenue Code (Section 504).

The historic basis for such rules is the prohibition on "unreasonably long" accumulations by trusts (originally related to the application of the Rule Against Perpetuities to private trusts), designed to protect life beneficiaries. M. Fremont-Smith, Foundations and Government (1965) 90, 128. It is not clear how such a general requirement has resulted in an inflexible rule for the twice-annual distribution of income.

Since one duty of a trustee (Section 5562) is the accomplishment of the charitable purposes for which he holds funds, which cannot occur without the distribution of income, the staff is of the opinion that such specific requirements for periodic distributions are unnecessary.

#### § 5564. Attorney General supervision

Section 5564 is the same as existing Section 505 (other than the arrangement in subdivisions) except for the deletion of property held subject to any "public" trust from the language. No case or other authority has been found indicating that any distinction of substance exists between public and charitable trusts. This is not surprising in view of the current judicial definition of "charitable" as "promoting the welfare of mankind at large, or of a community, or of some class forming a part of it indefinite as to numbers and individuals." Lynch v. Spilman, 67 Cal.2d 251, 260-261 (1967).

The staff also considered changing existing language to limit the scope of the Attorney General investigation to the extent necessary to ascertain whether the nonprofit corporation has failed to comply with its trusts or has departed from its purposes. However, the Attorney General is vested at common law with a broad power to superintend management of all charities. People v. Cogswell, 113 C. 129 (1896). The enactment of the predecessor of Section 9505 did not limit that power but merely restated it with regard to nonprofit corporations and added the mandatory duty to commence an action against corporations in certain situations. Brown v. Memorial Nat. Home Foundation, 162 Cal. App.2d 513, 537 (1958). In light of this history, the change was not made.

The Commission has requested the staff to consider the relationship of this section to the Uniform Supervision of Trustees for Charitable Purposes Act (Govt. Code §§ 12580-12597, attached as Exhibit III to this memorandum)("the Act"), the expansion of the section to cover entities other than nonprofit corporations, and relocation of the section.

The inherent supervisory powers of the Attorney General over charitable assets are not limited to nonprofit corporations. See People v. Cogswell, 113 C. 129 (1896); Estate of Quinn, 156 Cal. App.2d 684 (1958). It would thus be possible to expand the coverage of this section to, for example, "all individuals, groups, corporations, or other legal entities holding assets subject to a charitable trust" (see Govt. Code § 12582) without increasing the existing scope of the Attorney General's authority.

Were this change made, placement of the expanded section in the General Nonprofit Corporation Code would be inappropriate. As no general collection of statutory provisions relating to charities or charitable trusts exists in any code, it would be logical to place the section with the Act, or adjacent to it, in that portion of the Government Code dealing with the Attorney General (Govt. Code §§ 12500-12612).

The primary purpose of the Act is to provide information to the Attorney General regarding charitable fund management. W. Howland, The History of the Supervision of Charitable Trusts and Corporations in California, 13 U.C.L.A.L. Rev. 1029, 1032 (1966). The Act applies only to those entities already subject to the supervision of the Attorney General (Section 12581), specifically exempts certain types of organizations from its coverage (Section 12583: religious, educational, government, hospital, cemetery corporation), and provides for discretionary rather than mandatory enforcement action by the Attorney General (Section 12591). In short, the Act is simply a reporting procedure to aid the Attorney General in exercising existing substantive supervisory authority (see Section 12591).

Because of the limited nature of the authority granted (to require disclosure of information) and the coverage exceptions (of entities for whom reporting to the Attorney General would be either unnecessary or inappropriate) in the Act, the staff does not recommend placement of existing Section 9505 in the Act itself. If the Commission determines

that the section should be expanded and moved, the staff believes that it should become Section 12598 (Supervisory authority) and 12599 (Enforcement proceedings) of a new Article 7.5 of Chapter 5, Part 2, Division 3, Title 2 of the Government Code.

The staff does not believe that expansion of the section is necessary. The common law power of the Attorney General over all charities appears to be uncontested; there have been no successful contentions that the enactment of Section 9505 (and its predecessor) has reduced the scope of that inherent authority. If there is no expansion, there should be no relocation.

The section, as now worded, does represent a codification of only a portion of the authority of the Attorney General. The staff does not view such incompleteness as a defect of sufficient significance to compel revision and relocation of the section, but it also has no objections to a Commission decision to revise and move the statute. While some future reader of legislative intent might be tempted to see in the revised section a limitation on the inherent common law powers of the Attorney General, this could be avoided by an appropriate Comment.

#### § 5570. Establishment

This section continues the authority (Section 10250) to set up common trust funds only for nonprofit corporations with charitable purposes and to allow investments only on behalf of the establishing corporation and affiliated organizations. Some states extend the establishing authority to all nonprofit corporations and yet restrict the investment power to the establishing corporation alone. Pa. Stat. Ann. tit. 15, § 7581 (1972).

Proposed Section 5570 neither widens nor restricts the existing authority to establish and utilize such funds as there are no apparent significant reasons to change the status quo. The language of Section 10250 has been simplified in the new section.

Respectfully submitted,

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EXHIBIT I

[New York Not-for-Profit Corporation Law]

**N-PCL**

**§ 501. Stock and shares prohibited; membership certificate authorized.**

A corporation shall not have stock or shares or certificates for stock or for shares, but may issue nontransferable membership certificates or cards to evidence membership, whether or not connected with any financial contribution to the corporation, as provided in section 601 (Members). The fact that the corporation is a not-for-profit corporation, and that the membership certificate or card is non-transferable shall be noted conspicuously on the face or back of each such certificate or card.

**N-PCL**

**§ 502. Members' capital contributions.**

(a) The certificate of incorporation may provide that members, upon or subsequent to admission, shall make capital contributions in the amount specified therein. The requirement of a capital contribution may apply to all members, or to the members of a single class, or to members of different classes in different amounts or proportions.

(b) A member's capital contribution shall consist of money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the corporation shall be conclusive.

(c) Neither obligations of the member for future payments nor future services shall constitute payment or part payment of a member's capital contribution.

(d) A member's capital contribution shall be evidenced by a capital certificate which shall be non-transferable, except that the certificate of incorporation of a Type A corporation may provide that its capital certificates, or some of them, may be transferable to other members with consent of the corporation upon specified terms and conditions.

(e) A member's capital contribution shall not be repaid or redeemed by the corporation except upon dissolution of the corporation or upon redemption of the capital certificate as provided in this chapter. A corporation may provide in its certificate of incorporation that its capital certificates, or

some of them, shall be redeemable, in whole or in part, at the option of the corporation only, at such price or prices (not to exceed the amount of the capital contribution), within such period or periods, and on such terms and conditions, not inconsistent with this chapter, as are stated in the certificate of incorporation.

## **N-PCL**

### **§ 503. Capital certificates.**

(a) Each capital certificate shall be signed by the chairman or vice-chairman of the board or the president or a vice-president and the secretary or an assistant secretary or the treasurer or an assistant treasurer of the corporation, and may be sealed with the seal of the corporation or a facsimile thereof. The signatures of the officers upon a certificate may be facsimiles if the certificate is countersigned by a transfer agent or registered by a registrar other than the corporation itself or its employee. In case any officer who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer before such certificate is issued it may be issued by the corporation with the same effect as if he were such officer at the date of issue.

(b) Each capital certificate shall when issued state upon the face thereof:

(1) That the corporation is a Type \_\_\_\_\_ corporation under section 113 or section 402 of the New York Not-for-Profit Corporation Law.

(2) The name of the member to whom issued.

(3) The amount of the member's capital contribution evidenced by such certificate.

(4) If appropriate, that the corporation is a Type A corporation, and that its certificate of incorporation provides that the capital certificate is transferable to other members with the consent of the corporation.

(c) The fact that the corporation is a not-for-profit corporation, and that the capital certificate is non-transferable or is transferable to other members, with the consent of the corporation, shall be noted conspicuously on the face or back of each such certificate.

§ 504. Subventions.

(a) The certificate of incorporation may provide that the corporation shall be authorized by resolution of the board to accept subventions from members or non-members on terms and conditions not inconsistent with this chapter, and to issue certificates therefor. Subvention certificates shall be non-transferable unless such resolution provides that they shall be transferable, either at will or subject to specified restrictions.

(b) A subvention shall consist of money or other property, tangible or intangible, actually received by the corporation or expended for its benefit or for its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the corporation shall be conclusive.

(c) The rights of holders of subvention certificates shall at all times be subordinate to the rights of creditors of the corporation.

(d) The resolution of the board may provide that holders of subvention certificates shall be entitled to a fixed or contingent periodic payment out of the corporate assets equal to a percentage of the original amount or value of the subvention, but such payment shall not exceed two-thirds of the maximum interest rate authorized pursuant to section 5-501 of the general obligations law.

(e) The resolution of the board may provide that a subvention shall be redeemable, in whole or in part, at the option of the corporation at such price or prices (not to exceed the original amount or value of the subvention plus any periodic payments due or accrued thereon), within such period or periods, and on such terms and conditions, not inconsistent with this chapter, as are stated in the resolution.

(f) The resolution of the board may provide that holders of all or some subvention certificates shall have the right to require the corporation after a specified period of time to redeem such certificates, in whole or in part, at a price or prices that do not exceed the original amount or value of the subvention plus any periodic payments due or accrued thereon, upon an affirmative showing that the financial condition of the corporation will permit the required payment to be made without impairment of its operations or injury to its creditors. The right to require redemption may in addition be conditioned upon the occurrence of a specified event. For the purpose of enforcing their rights under this paragraph, holders of subvention certificates shall be entitled to inspect the books and records of the corporation.

(g) Holders of subvention certificates, upon dissolution of the corporation, shall be entitled, after the claims of creditors have been satisfied, to a repayment of the original amount or value of the subvention plus any periodic payments due or accrued thereon, unless a lesser sum is specified in the certificate of incorporation or the resolution of the board concerning such subvention.

## N-PCL

### § 505. Subvention certificates.

(a) Each subvention certificate shall be signed by the chairman or a vice-chairman of the board or the president or a vice-president and the secretary or an assistant secretary or the treasurer or an assistant treasurer of the corporation, and may be sealed with the seal of the corporation or a facsimile thereof. The signatures of the officers upon a certificate may be facsimiles if the certificate is countersigned by a transfer agent or registered by a registrar other than the corporation itself or its employees. In case any officer who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer before such certificate is issued, it may be issued by the corporation with the same effect as if he were such officer at the date of issue.

(b) Each subvention certificate shall when issued state upon the face thereof:

(1) That the corporation is a Type ..... corporation under section 113 or section 402 of the New York Not-for-Profit Corporation Law.

(2) The name of the person or persons to whom issued.

(3) The amount of the subvention evidenced by such certificate.

(4) The amount of the periodic payment thereon, if any, authorized by the resolution of the board.

(5) If appropriate, that the certificate is redeemable and a summary of the conditions for redemption at the option of the corporation or of the holder.

(6) If appropriate, that the certificate is transferable, either at will or subject to specified restrictions.

(c) The fact that the corporation is a not-for-profit corporation and, where appropriate, that the certificate is transferable at will or subject to restrictions, shall be noted conspicuously on the face or back of each such certificate.

**§ 506. Bonds and security interests.**

(a) No corporation shall issue bonds except for money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the corporation shall be conclusive.

(b) A corporation may pay reasonable interest on its bonds, may issue its bonds at a reasonable discount and may pay a reasonable premium for the redemption thereof prior to maturity, but the holders of its bonds shall not be entitled at any time to receive any part of the income or profit of the corporation nor at maturity to receive more than the principal sum thereof plus interest due and accrued thereon. In the absence of fraud in the transaction, the judgment of the board as to the reasonableness of any such interest, discount or premium shall be conclusive. However, with respect to bonds not a part of a public offering, notwithstanding the terms of the instrument, no member of a corporation shall be entitled to receive, directly or indirectly, as a holder or beneficiary of such bond, prior to maturity or redemption more than simple interest thereon at a rate equal to the higher of (1) the maximum interest authorized pursuant to section 5-501 of the general obligations law or (2) one percent over the prime rate of interest then generally prevailing on the interest due date in the Federal Reserve District of New York, nor at maturity or redemption, more than the principal sum thereof plus any interest, not exceeding the maximum interest herein specified, due and accrued thereon.

(c) A corporation may, in its certificate of incorporation or by-laws, confer upon the holders of any bonds issued or to be issued by the corporation, rights to inspect the corporate books and records and, upon default of interest or principal, to vote in the election of directors. The certificate of incorporation or the by-laws may apportion the number of votes that may be cast with respect to bonds on the basis of the amount of bonds held.

(d) The board may authorize any mortgage or pledge of, or the creation of a security interest in, all or any part of the corporation's personal property, or any interest therein. Unless the certificate of incorporation provides otherwise, no vote or consent of the members shall be required to approve such action by the board.

**N-PCL**

**§ 507. Fees, dues and assessments; fine and penalties.**

(a) If authorized by its certificate of incorporation and subject to any limitations stated either in the certificate or in the by-laws, a corporation may levy initiation fees, dues and assessments on its members, whether or not they are voting members, and may impose reasonable fines or other penalties upon its members for violations of its rules and regulations.

(b) Initiation fees, dues or assessments may be levied on all classes of members alike or in different amounts or proportions for different classes of members, as the certificate of incorporation or the by-laws may provide, but in all cases the fees, dues and assessments payable by members of one class shall be determined upon the same basis.

(c) The certificate of incorporation or the by-laws may contain such provisions as are deemed necessary to enforce the collection of fees, dues, assessments, fines or other penalties, including provisions for the termination of membership, upon reasonable notice, for non-payment of such fees, dues, assessments, fines or other penalties, and provisions for reinstatement of membership.

(d) Subject to the provisions of this chapter, the certificate of incorporation may provide that members paying initiation fees, dues or assessments shall, upon dissolution of the corporation, have distributive rights in its assets. The distributive rights may be different for different classes of members, but in all cases the rights of members of one class shall be the same.

**N-PCL**

**§ 514. Transfer of corporate property to a trustee.**

(a) Any corporation holding or receiving assets under section 513 (Administration of assets received for specific purposes) may, by appropriate action of its board, transfer any such assets to a corporate trustee, which shall be a bank and trust company or a trust company or fund incorporated under the laws of the state of New York or a national banking association having fiduciary powers and having its principal office in this state, as trustee and with like investment restrictions.

(1) Upon such transfer, which may be revocable or irrevocable, the board of the corporation shall be relieved of all

liability for the administration of such assets for as long as the latter are administered by the corporate trustees.

(2) Such corporate trustee shall pay, at least semi-annually or at more frequent intervals if so agreed, the net income of such assets, which may include so much of the realized appreciation of principal, within the limitations specified in paragraphs (d) and (e) of section 513 with respect to assets retained by the corporation, as the corporate trustee may deem prudent, to the corporation for use and application to the specific purpose or purposes for which the assets were received by the corporation.

(b) The certificate of incorporation may provide for the appointment of individual or corporate trustees for any or all of the corporate property. Such appointment may be made by an instrument which shall also state the purposes of the corporation for which such property is to be held, and may confer on such trustees such of the powers, duties or obligations of the directors in relation to the care, custody or management of such property as may be deemed appropriate.

(c) The designation of an individual or corporate trustee for corporate property shall not relieve any director of his duty to the corporation under section 717 (Duty of directors and officers) to exercise due care in the selection of the trustee and in the continuation or termination of the trust.

## N-PCL

**§ 515. Dividends prohibited: certain distributions of cash or property authorized.**

(a) A corporation shall not pay dividends or distribute any part of its income or profit to its members, directors, or officers.

(b) A corporation may pay compensation in a reasonable amount to members, directors, or officers for services rendered, and may make distributions of cash or property to members upon dissolution or final liquidation as permitted by this chapter.

(c) A corporation may confer benefits upon members or non-members in conformity with its purposes, may redeem its capital certificates or subvention certificates, and may make other distributions of cash or property to its members or former members, directors, or officers prior to dissolution or final liquidation, as authorized by this article, except when the corporation is currently insolvent or would thereby be made insolvent or rendered unable to carry on its corporate purposes, or when the fair value of the corporation's assets remaining after such conferring of benefits, or redemption, or other distribution would be insufficient to meet its liabilities.

§ 516. Distributions to members upon termination of membership.

(a) Except as provided in this chapter or the certificate of incorporation or the by-laws, the interest of a member in the property of a corporation shall terminate upon the termination of his membership, whether by expiration of the term of membership, or by the death, voluntary withdrawal, or expulsion of the member, or otherwise. Such termination shall be without prejudice to his rights, if any, as holder of a capital or subvention certificate.

(b) In the event of a termination of membership, whether voluntary or involuntary, and subject to any restrictions contained in this chapter or the certificate of incorporation or the by-laws, a corporation may at its option thereafter call for redemption any capital certificate or certificates held by such former member, and redeem the same upon payment of a sum of money equal to the redemption price thereof if such certificates are by their terms redeemable, or upon payment of a sum of money equal to the amount of the capital contribution evidenced by such certificates if they are not by their express terms redeemable.

(c) If a member who would upon dissolution of the corporation have distributive rights in its assets under paragraph (d) of section 507 (Fees, dues and assessments; fines and penalties) is expelled other than for cause pursuant to a provision of the certificate of incorporation or by-laws authorizing such expulsion, and the corporation is dissolved within a period of five years after the date of such expulsion, the expelled member shall be entitled to share in the distribution of assets in the same manner as other members of the same class entitled to share at that time, except that his share shall be charged with any arrearages and all dues and assessments which he would have paid if he had remained a member, plus interest on all such items.

(d) Nothing in this section shall authorize a corporation to make a distribution of cash or property to a former member in contravention of the provisions of section 515 (Dividends prohibited; certain distributions of cash or property authorized).

## Exhibit II

## [Pennsylvania Corporation Not-for-profit Code]

**§ 7541. Capital contributions of members**

(a) **General rule.**—A nonprofit corporation organized on a non-stock basis may provide in its bylaws that members, upon or subsequent to admission, shall make capital contributions. The amount shall be specified in, or fixed by the board of directors or other body pursuant to authority granted by, the bylaws. The requirement of a capital contribution may apply to all members, or to the members of a single class, or to members of different classes in different amounts or proportions.

(b) **Consideration receivable.**—The capital contribution of a member shall consist of money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board of directors or other body as to the value of the consideration received by the corporation shall be conclusive.

(c) **Evidence of contribution.**—The capital contribution of a member shall be recorded on the books of the corporation and may be evidenced by a written instrument delivered to the member, but such instrument shall not be denominated a "share certificate" or by any other word or term implying that the instrument is a share certificate subject to section 7752 of this title (relating to organization on a stock share basis).

(d) **Transferability of interest.**—Unless otherwise provided in the bylaws, the capital contribution of a member shall not be transferable.

(e) **Repayment of contribution.**—The capital contribution of a member shall not be repaid by the corporation except upon dissolution of the corporation or as provided in this article. A corporation may provide in its bylaws that its capital contributions, or some of them, shall be repayable, in whole or in part, at the option of the corporation only, at such amount or amounts (not to exceed the amount of the capital contribution), within such period or periods, and on such terms and conditions, not inconsistent with this article, as are stated in, or fixed by the board of directors or other body pursuant to authority granted by, the bylaws.

**§ 7542. Subventions**

(a) **General rule.**—The bylaws may provide that the corporation shall be authorized by resolution of the board of directors or other body to accept subventions from members or nonmembers on terms and conditions not inconsistent with this article, and to issue certificates therefor. The resolution of the board or other body may provide that holders of subvention certificates shall be entitled to a fixed or contingent periodic payment out of the corporate assets equal to a percentage of the original amount or value of the subvention. The rights of holders of subvention certificates shall at all times be subordinate to the rights of creditors of the corporation.

(b) **Consideration receivable.**—A subvention shall consist of money or other property, tangible or intangible, actually received

by the corporation or expended for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board of directors or other body as to the value of the consideration received by the corporation shall be conclusive.

**(c) Form of certificate.**—Each subvention certificate shall be signed by two duly authorized officers of the corporation, and may be sealed with the seal of the corporation or a facsimile thereof. The signatures of the officers upon a certificate may be facsimiles if the certificate is countersigned by a transfer agent or registered by a registrar other than the corporation itself or its employees. In case any officer who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer before such certificate is issued, it may be issued by the corporation with the same effect as if he were such officer at the date of issue. The fact that the corporation is a nonprofit corporation shall be noted conspicuously on the face or back of each certificate.

**(d) Transferability of subvention.**—Subvention certificates shall be nontransferable unless the resolution of the board of directors or other body shall provide that they shall be transferable either at will or subject to specified restrictions.

**(e) Redemption at option of corporation.**—The resolution of the board of directors or other body may provide that a subvention shall be redeemable, in whole or in part, at the option of the corporation at such price or prices (not to exceed the original amount or value of the subvention plus any periodic payments due or accrued thereon), within such period or periods, and on such terms and conditions, not inconsistent with this article, as are stated in the resolution.

**(f) Redemption at option of holders.**—The resolution of the board of directors or other body may provide that holders of all or some subvention certificates shall have the right to require the corporation after a specified period of time to redeem such certificates, in whole or in part, at a price or prices that do not exceed the original amount or value of the subvention plus any periodic payments due or accrued thereon, upon an affirmative showing that the financial condition of the corporation will permit the required payment to be made without impairment of its operations or injury to its creditors. The right to require redemption may in addition be conditioned upon the occurrence of a specified event. For the purpose of enforcing their rights under this subsection, holders of subvention certificates shall be entitled to inspect the books and records of the corporation.

**(g) Rights of holders on dissolution.**—Holders of subvention certificates, upon dissolution of the corporation, shall be entitled, after the claims of creditors have been satisfied, to repayment of the original amount or value of the subvention plus any periodic payments due or accrued thereon, unless a lesser sum is specified in the resolution of the board of directors or other body concerning such subvention.

### **§ 7543. Debt and security interests**

(a) **General rule.**—No corporation shall issue bonds or other evidences of indebtedness except for money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud in the transaction, the judgment of the board of directors or other body as to the value of the consideration received by the corporation shall be conclusive.

(b) **Creation of lien on personal property.**—The board of directors or other body may authorize any mortgage or pledge of, or the creation of a security interest in, all or any part of the personal property of the corporation, or any interest therein. Unless otherwise restricted in the bylaws no vote or consent of the members shall be required to make effective such action by the board or other body.

### **§ 7544. Usury not a defense**

(a) **General rule.**—No nonprofit corporation shall plead or set up usury, or the taking of more than the lawful rate of interest, as a defense to any action brought against it to recover damages on, or to enforce payment of, or to enforce any other remedy on, any mortgage, bond, note or other obligation executed or effected by the corporation.

(b) **Nonqualified foreign corporations.**—The provisions of this section shall extend to all mortgages, bonds, notes or other obligations executed or effected in this Commonwealth by a nonqualified foreign corporation and to mortgages and other obligations executed by nonqualified foreign corporations affecting real property situated in this Commonwealth.

### **§ 7545. Fees, dues and assessments**

(a) **General rule.**—A nonprofit corporation may levy dues or assessments, or both, on its members, if authority to do so is conferred by the bylaws, subject to any limitations therein contained. Such dues or assessments, or both, may be imposed upon all members of the same class either alike or in different amounts or proportions, and upon a different basis upon different classes of members. Members of one or more classes may be made exempt from either dues or assessments, or both, in the manner or to the extent provided in the bylaws.

(b) **Amount and method of collection.**—The amount of the levy and method of collection of such dues or assessments, or both, may be fixed in the bylaws, or the bylaws may authorize the board of directors or other body to fix the amount thereof from time to time, and make them payable at such time and by such methods of collection as the board of directors or other body may prescribe.

(c) **Enforcement of payment.**—A nonprofit corporation may make bylaws necessary to enforce the collection of such dues or assessments, including provisions for the termination of membership, upon reasonable notice, for nonpayment of such dues or assessments, and for reinstatement of membership.

**§ 7551. Transfer of trust or other assets to institutional trustee**

(a) **General rule.**—Any nonprofit corporation holding or receiving assets under section 7549 of this title (relating to authority to take and hold trust property) may, by appropriate action of its board of directors or other body, transfer, which transfer may be either revocable or irrevocable, any such assets to a corporate trustee, which shall be a bank and trust company or a trust company incorporated under the laws of this Commonwealth or a national banking association having fiduciary powers and having its principal office in this Commonwealth, as trustee and with like investment restrictions. In like manner the corporation may transfer, which transfer shall be revocable, any other part of its assets to such a corporate trustee, subject to the same powers, restrictions and obligations with respect to investment as are applicable to the corporation itself.

(b) **Relief from liability.**—Upon such transfer the board of directors or other body of the corporation shall be relieved of all liability for the administration of such assets for as long as such assets are administered by the corporate trustee.

(c) **Amount and frequency of payment.**—Such corporate trustee shall pay, at least semi-annually or at more frequent intervals if so agreed, the net income from such assets, which may include so much of the realized appreciation of principal as the board of directors or other body of the corporation may deem prudent, to the corporation for use and application to the purpose or purposes for which the assets were received by the corporation.

**§ 7553. Dividends prohibited; compensation and certain payments authorized**

(a) **General rule.**—A nonprofit corporation shall not pay dividends or distribute any part of its income or profits to its members, directors, or officers.

(b) **Reasonable compensation for services.**—A nonprofit corporation may pay compensation in a reasonable amount to members, directors, or officers for services rendered.

(c) **Certain payments authorized.**—A nonprofit corporation may confer benefits upon members or nonmembers in conformity with its purposes, may repay capital contributions, and may redeem its subvention certificates or evidences of indebtedness, as authorized by this article, except when the corporation is currently insolvent or would thereby be made insolvent or rendered unable to carry on its corporate purposes, or when the fair value of the assets of the corporation remaining after such conferring of benefits, payment or redemption would be insufficient to meet its liabilities. A nonprofit corporation may make distributions of cash or property to members upon dissolution or final liquidation as permitted by this article.

**§ 7581. Establishment or use of common trust funds authorized**

(a) **General rule.**—Every nonprofit corporation may establish and maintain one or more common trust funds, the assets of which shall be held, invested and reinvested by the corporation itself or by a corporate trustee to which the assets have been transferred pursuant to section 7551 of this title (relating to transfer of trust or other assets to institutional trustee). Upon the payment by the corporate trustee to the nonprofit corporation of the net income from such assets, for use and application to the several participating interests in such common trust fund, the proportionate participation of each interest in such net income shall be designated by the corporate trustee. The nonprofit corporation may, at any time, withdraw the whole or part of any participating interest in such common trust fund for distribution by it as provided in this subchapter.

(b) **Limitations in trust instrument.**—Nothing contained in this section shall be construed to authorize the corporation to invest assets of a trust or fund in any such common trust fund contrary to any specific limitation or restriction contained in the trust instrument, nor to limit or restrict the authority conferred upon the corporation with respect to investments by any such trust instrument.

(c) **Effect of good faith mistakes.**—No mistakes made in good faith, and in the exercise of due care and prudence, in connection with the administration of any such common trust fund, shall be held to exceed any power granted to or violate any duty imposed upon the corporation, if, promptly after the discovery of the mistake, the corporation takes such action as may be practicable under the circumstances to remedy the mistake.

EXHIBIT III

ARTICLE 7

Uniform Supervision of Trustees for Charitable Purposes Act

[Added by Stats 1959 ch 1258 § 2, effective June 30, 1959.]

Former Article 7, consisting of §§ 12580-12596, was added by Stats 1955 ch 1820 § 1 and repealed by Stats 1959 ch 1258 § 1, effective June 30, 1959.

- § 12580. Citation of article
- § 12581. Corporations and trustees to which article applicable
- § 12582. "Trustee"
- § 12582. i. "Charitable corporation"
- § 12583. Governmental entities, corporations, organizations and persons to which article inapplicable
- § 12584. Establishment and maintenance of register of charitable corporations and trustees: Investigation
- § 12585. Duty of charitable corporation or trustee to file copy of instrument providing for title, powers or duties
- § 12586. Duty of charitable corporation or trustee to file reports: Rules and regulations: Copy of account filed in court as report: Time for filing first report
- § 12587. Attorney General's power to make additional rules and regulations
- § 12588. Investigation of transactions and relationships of corporations and trustees: Requiring appearance and production of books, etc.
- § 12589. Order for attendance: Contents: Review
- § 12590. Availability of register, copies of instruments and reports for public inspection
- § 12591. Proceedings to secure compliance with article and to invoke jurisdiction of court: Additional powers and duties of Attorney General: Effect of article on court's jurisdiction
- § 12592. Application of article regardless of contrary provision of instrument
- § 12593. Furnishing Attorney General with copies of documents
- § 12594. Filing with Attorney General list of applications for exemption from taxation
- § 12595. Construction of act
- § 12596. Time within which Attorney General may bring action to enforce charitable trust
- § 12597. Provision in judgment for payment of expense incurred by state

§ 12580. Citation of article

This article may be cited as the Uniform Supervision of Trustees for Charitable Purposes Act.

**§ 12581. Corporations and trustees to which article applicable**  
This article applies to all charitable corporations and trustees holding property for charitable purposes over which the State or the Attorney General has enforcement or supervisory powers.

**§ 12582. "Trustee"**

"Trustee" means (a) any individual group of individuals, corporation, or other legal entity holding property in trust pursuant to any charitable trust, (b) any corporation which has accepted property to be used for a particular charitable corporate purpose as distinguished from the general purposes of the corporation, and (c) a corporation formed for the administration of a charitable trust, pursuant to the directions of the settlor or at the instance of the trustee.

**§ 12582.1. "Charitable corporation"**

"Charitable corporation" means any nonprofit corporation organized under the laws of this State for charitable or eleemosynary purposes and any similar foreign corporation doing business or holding property in this State for such purposes.

**§ 12583. Governmental entities, corporations, organizations and persons to which article inapplicable**

This article does not apply to the United States, any state, territory, or possession of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or to any of their agencies or governmental subdivisions, to any religious corporation sole or other religious corporation or organization which holds property for religious purposes, or to any officer, director, or trustee thereof who holds property for like purposes, to a cemetery corporation regulated under Chapter 19 of Division 3 of the Business and Professions Code, or to a charitable corporation organized and operated primarily as a religious organization, educational institution or hospital.

**§ 12584. Establishment and maintenance of register of charitable corporations and trustees: Investigation**

The Attorney General shall establish and maintain a register of charitable corporations and trustees subject to this article and of the particular trust or other relationship under which they hold property for charitable purposes and, to that end, may conduct whatever investigation is necessary, and shall obtain from public records, court officers, taxing authorities, trustees, and other sources, whatever information, copies of instruments, reports, and records are needed for the establishment and maintenance of the register.

**§ 12585. Duty of charitable corporation or trustee to file copy of instrument providing for title, powers or duties**

Every charitable corporation and trustee subject to this article who has received property for charitable purposes shall file with the Attorney General, within six months after any part of the income or principal is authorized or required to be applied to a charitable purpose, a copy of the articles of incorporation or other instrument providing for his title, powers or duties. If any part of the income or principal is authorized or required to be applied to a charitable purpose at the time this article takes effect, the filing shall be made within six months thereafter.

**§ 12586. Duty of charitable corporation or trustee to file reports: Rules and regulations: Copy of account filed in court as report: Time for filing first report**

(a) Except as otherwise provided and except corporate trustees which are subject to the jurisdiction of the Superintendent of Banks of the State of California or to the Comptroller of Currency of the United States, every charitable corporation and trustee subject to this article shall, in addition to filing copies of the instruments previously required, file with the Attorney General periodic written reports, under oath, setting forth information as to the nature of the assets held for charitable purposes and the administration thereof by the corporation or trustee, in accordance with rules and regulations of the Attorney General.

(b) The Attorney General shall make rules and regulations as to the time for filing reports, the contents thereof, and the manner of executing and filing them. He may classify trusts and other relationships concerning property held for a charitable purpose as to purpose, nature of assets, duration of the trust or other relationship, amount of assets, amounts to be devoted to charitable purposes, nature of trustee, or otherwise, and may establish different rules for the different classes as to time and nature of the reports required to the ends (1) that he shall receive reasonably current, periodic reports as to all charitable trusts or other relationships of a similar nature, which will enable him to ascertain whether they are being properly administered, and (2) that periodic reports shall not unreasonably add to the expense of the administration of charitable trusts and similar relationships. The Attorney General may suspend the filing of reports as to a particular charitable trust or relationship for a reasonable, specifically designated time upon written application of the trustee filed with the Attorney General and after the Attorney General has filed in the register of charitable trusts a written statement that the interests of the beneficiaries will not be prejudiced thereby and that periodic reports are not required for proper supervision by his office.

(c) A copy of an account filed by the trustee in any court having jurisdiction of the trust or other relationship, if the account substantially complies with the rules and regulations of the Attorney General, may be filed as a report required by this section.

(d) The first report for a trust or similar relationship hereafter established, unless the filing thereof is suspended as herein provided, shall be filed not later than four (4) months and fifteen (15) days following the close of the first calendar or fiscal year in which any part of the income or principal is authorized or required to be applied

to a charitable purpose. If any part of the income or principal of a trust previously established is authorized or required to be applied to a charitable purpose at the time this article takes effect, the first report shall be filed at the close of the calendar or fiscal year in which it was registered with the Attorney General or not later than four (4) months and fifteen (15) days following the close of such calendar or fiscal period.

**§ 12587. Attorney General's power to make additional rules and regulations**

The Attorney General may make additional rules and regulations necessary for the administration of this article.

**§ 12588. Investigation of transactions and relationships of corporations and trustees: Requiring appearance and production of books, etc.**

The Attorney General may investigate transactions and relationships of corporations and trustees subject to this article for the purpose of ascertaining whether or not the purposes of the corporation or trust are being carried out in accordance with the terms and provisions of the articles of incorporation or other instrument. He may require any agent, trustee, fiduciary, beneficiary, institution, association, or corporation, or other person to appear, at a named time and place, in the county designated by the Attorney General, where the person resides or is found, to give information under oath and to produce books, memoranda, papers, documents of title, and evidence of assets, liabilities, receipts, or disbursements in the possession or control of the person ordered to appear.

**§ 12589. Order for attendance: Contents: Review**

When the Attorney General requires the attendance of any person, as provided in Section 12588, he shall issue an order setting forth the time when and the place where attendance is required and shall cause the same to be delivered to or sent by registered mail to the person at least 14 days before the date fixed for attendance. Such order shall have the same force and effect as a subpoena and, upon application of the Attorney General, obedience to the order may be enforced by the Superior court in the county where the person receiving it resides or is found, in the same manner as though the notice were a subpoena. The court, after hearing, for cause, and upon application of any person aggrieved by the order, shall have the right to alter, amend, revise, suspend or postpone all or any part of its provisions.

**§ 12590. Availability of register, copies of instruments and reports for public inspection**

Subject to reasonable rules and regulations adopted by the Attorney General, the register, copies of instruments, and the reports filed with the Attorney General shall be open to public inspection. The Attorney General shall withhold from public inspection any instrument so filed whose content is not exclusively for charitable purposes.

**§ 12591. Proceedings to secure compliance with article and to invoke jurisdiction of court: Additional powers and duties of Attorney General: Effect of article on court's jurisdiction**

The Attorney General may institute appropriate proceedings to secure compliance with this article and to invoke the jurisdiction of the court. The powers and duties of the Attorney General provided in this article are in addition to his existing powers and duties. Nothing in this article shall impair or restrict the jurisdiction of any court with respect to any of the matters covered by it, except that no court shall have jurisdiction to modify or terminate any trust of property for charitable purposes unless the Attorney General is a party to the proceedings.

**§ 12592. Application of article regardless of contrary provision of instrument**

This article shall apply regardless of any contrary provisions of any instrument.

**§ 12593. Furnishing Attorney General with copies of documents**

Every person who offers for probate any instrument which establishes a testamentary trust of property for charitable purposes or who records in any county or city and county any inter vivos transfer of property for charitable purposes shall furnish a copy of such document to the Attorney General. The custodian of the records of a court having jurisdiction of probate matters or of charitable trusts shall furnish such copies of papers, records and files of his office relating to the subject of this article as the Attorney General requires.

**§ 12594. Filing with Attorney General list of applications for exemption from taxation**

Every officer, agency, board, or commission of this State receiving applications for exemption from taxation of any corporation, charitable trust or similar relationship in which the corporation or trustee is subject to this article shall annually file with the Attorney General a list of all applications received during the year.

**§ 12595. Construction of act**

This act shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact it.

**§ 12596. Time within which Attorney General may bring action to enforce charitable trust**

Any action brought by the Attorney General against trustees or other persons holding property in trust for charitable purposes or against any charitable corporation or any director or officer thereof to enforce a charitable trust or to impress property with a trust for charitable purposes or to recover property or the proceeds thereof for and on behalf of any charitable trust or corporation, may be brought at any time within ten (10) years after the cause of action shall have accrued.

**§ 12597. Provision in judgment for payment of expense incurred by state**

In any proceeding brought by the Attorney General to secure compliance with the provisions of Sections 12584 to 12587, inclusive, or any regulation issued pursuant thereto, the judgment, if in favor of the state, shall provide that the person having the responsibility or duty to comply with such provisions on behalf of any charitable trust or charitable corporation, shall pay the reasonable expense necessarily incurred by the state in the investigation and prosecution of such action.

Rough Outline

GENERAL NONPROFIT CORPORATION LAW

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APPENDIX

Part 1 of Division 2 of the Corporations Code (repealed)  
General Nonprofit Corporation Law (§§ 9000-9802)

Tentatively Approved  
February 1976  
Renumbered May 1976

CHAPTER 5. CORPORATE FINANCE

Article 1. General Provisions

§ 5500. Levy of dues and assessments

5500. (a) The articles or bylaws may authorize dues or assessments or both to be levied upon all members or classes of membership alike, or in different amounts or proportions or upon a different basis upon different members or classes of membership and may exempt some members or classes of membership from either dues or assessments or both.

(b) The articles or bylaws may fix the amount and method of collection of dues or assessments or both, or may authorize the board of directors to fix the amount thereof from time to time, and make them payable at such times or intervals and upon such notice and by such methods as the directors may prescribe.

(c) The articles or bylaws may fix the amount and method of collection of charges owed to the nonprofit corporation.

(d) Dues, assessments, or charges, or all of them, may be made enforceable by action or by sale or forfeiture of membership, or both, upon reasonable notice.

Comment. Section 5500 augments Sections 5261(d) (liability of members to dues and assessments) and 5410 (authority of nonprofit corporations to levy dues and assessments).

Subdivision (a) continues the substance of the third sentence of former Section 9301.

Subdivision (b) continues the substance of the fourth sentence of former Section 9301.

Subdivision (c) is new.

Subdivision (d) continues the substance of the last sentence of former Section 9301 with the addition of a provision for the collection of charges owed to the nonprofit corporation in the manner of dues or assessments.

968/978

§ 5501

§ 5501. Levy of assessments

5501. (a) This section applies where a nonprofit corporation levies an assessment upon its members or any class of members in an amount in excess of three times the annual dues or regularly recurring annual assessment, whichever is greater, fixed for such members or class of members.

(b) A nonprofit corporation shall give written notice of an assessment described in subdivision (a) to each member subject to the assessment by mailing a copy of the articles, bylaw, or resolution of the board fixing the amount and terms of the assessment to the member at the address of the member appearing on the books of the nonprofit corporation for the purpose of notice.

(c) Each member subject to an assessment described in subdivision (a) may withdraw from membership by delivering to the nonprofit corporation at its principal executive office written notice of withdrawal within a period of 15 days from the giving of written notice of assessment by the nonprofit corporation pursuant to subdivision (b). The withdrawal shall be upon the same terms and conditions established by the nonprofit corporation for withdrawal from membership in the absence

of such an assessment and, upon withdrawal, the withdrawing member shall not be liable for such assessment.

Comment. Section 5501 is new.

The section protects a member from liability for extraordinary assessments, typically for major property, construction, or program additions by the nonprofit corporation. The limitation stated in subdivision (a) provides the nonprofit corporation with the opportunity to fix assessments in amounts bearing some reasonable relationship to annually recurring financial burdens of membership (such as for unexpected operating deficits) without the requirement that members be allowed to escape liability by withdrawal. The binding nature of assessments below the limitation is appropriate because the amount involved will necessarily be within the member's concept of the general financial consequences of membership.

This section does not prohibit a nonprofit corporation from adopting a bylaw restricting the right of a former member, after exercising his withdrawal right, to rejoin the organization.

968/979

§ 5504

§ 5504. Replacement of lost, stolen, or destroyed instruments

5504. (a) This section applies to a membership, capital, or subvention certificate, or a bond or other evidence of indebtedness which was issued by the nonprofit corporation or by any nonprofit corporation of which it is the lawful successor and which is alleged to have been lost, stolen, or destroyed.

(b) A nonprofit corporation may issue a new instrument to replace an instrument described in subdivision (a) and may require the owner of

the instrument described in subdivision (a) or the owner's legal representative to give the nonprofit corporation a bond (or other adequate security) sufficient to indemnify it against any claim that may be made against it (including any expense or liability) on account of the alleged loss, theft, or destruction of the instrument described in subdivision (a) or the issuance of the new instrument.

(c) If the nonprofit corporation refuses to replace an instrument described in subdivision (a), the owner of the instrument or the owner's legal representative may bring an action to require the nonprofit corporation to replace the instrument, subject to the following procedure:

(1) The action shall be brought in the superior court of the proper county.

(2) The court shall make an order requiring the nonprofit corporation to issue and deliver to the plaintiff a replacement instrument if the court is satisfied that (i) the plaintiff is the lawful owner of the instrument described in the complaint, (ii) the instrument has been lost, stolen, or destroyed, and (iii) no sufficient cause has been shown why a replacement instrument should not be issued.

(3) In its order, the court shall direct that, prior to the issuance and delivery to the plaintiff of the new instrument, the plaintiff give the nonprofit corporation such a bond (or other adequate security) as to the court appears sufficient to indemnify the nonprofit corporation against any claim that may be made against it (including any expense or liability) on account of the loss, theft, or destruction of the instrument described in subdivision (a) or the issuance of the new instrument.

Comment. Section 5504 is the same in substance as Section 419 (General Corporation Law). It continues provisions of former Sections 2481-2485, which were applicable to nonprofit corporations through former Section 9002.(/?)

Article 2. Capital Contributions

§ 5510. Capital contributions authorized

5510. (a) The articles or bylaws may provide that a nonprofit corporation is authorized by resolution of the board to require members, upon or subsequent to admission, to make capital contributions in the amount specified therein.

(b) The requirement of a capital contribution may apply to all members, or to the members of a single class, or to members of different classes in different amounts or proportions.

Comment. Sections 5510 through 5515 are new.

Former Section 9611 (General Nonprofit Corporation Law) authorized a nonprofit corporation to require contributions from its members, and that authority is continued in Section 5500 (levy of dues and assessments). Section 5510 authorizes a nonprofit corporation to require the payment by members of specific capital contributions; the following sections provide rules governing capital contributions (Sections 5511-5514). The concept and the rules are derived from Section 502 of the New York Not-for-Profit Corporation Law and Section 7541 of the Pennsylvania Corporation Not-for-profit Code.

§ 5511. Consideration

5511. A member's capital contribution may consist of such consideration as is determined from time to time by the board, or by the members if the articles or bylaws so provide, consisting of any or all

of the following: money paid, labor done, services actually rendered to or for the benefit of or in the formation or reorganization of the nonprofit corporation, debts or securities canceled, and tangible or intangible property actually received by the nonprofit corporation. Neither promissory notes of the member nor obligations for future services shall constitute full or part payment of a member's capital contribution. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the nonprofit corporation shall be conclusive.

Comment. See the Comment to Section 5510.

Section 5511 is adapted from Section 409, defining valid consideration for the issuance of shares by a corporation, which is a revision of former Section 1109 (General Corporation Law).

968/976

§ 5512

§ 5512. Redemption

5512. A member's capital contribution shall not be repaid or redeemed by the nonprofit corporation except upon dissolution of the nonprofit corporation or upon redemption of the capital contribution as provided in this chapter. The resolution of the board requiring the capital contribution may provide that the capital contributions, or some of them, are redeemable in whole or in part, at the option of the nonprofit corporation only, at such price or prices (not to exceed the amount of the capital contribution), within such period or periods, and

on such terms and conditions, not inconsistent with this chapter, as are stated in the resolution of the board.

Comment. See the Comment to Section 5510.

This section provides that redemption may occur only at the option of the nonprofit corporation; for similar provisions concerning redemption of stock in the General Corporation Law, see Section 402(b) and former Section 1101. It should be noted that this section incorporates by reference the protective provisions of Sections 5551 and 5552.

406/479

§ 5513

§ 5513. Capital certificates

5513. (a) The capital contribution of a member shall be recorded on the books of the nonprofit corporation and may be evidenced by a written capital certificate delivered to the member.

(b) Unless otherwise provided in the resolution of the board requiring the capital contribution, neither the capital contribution of a member nor the capital certificate evidencing such contribution shall be transferable.

Comment. See the Comment to Section 5510.

This section provides for optional issuance and transferability of capital certificates evidencing contributions. Sections 5513 and 5514 are derived from Section 503 of the New York Not-for-Profit Corporation Law and Section 7541 of the Pennsylvania Corporation Not-for-profit Code.

§ 5514. Contents of certificate

5514. There shall appear upon the face of each capital certificate the following information:

- (a) That the issuer is a nonprofit corporation.
- (b) That the capital contribution is nontransferable, if applicable.
- (c) That the capital contribution is redeemable, if applicable.

Comment. See the Comment to Section 5513.

For comparable provisions, see Section 5405 (membership certificates); see also Section 418(a) and former Sections 2401 and 2403 (General Corporation Law).

§ 5515. Officers' certificate

5515. Before a nonprofit corporation issues a capital certificate, an officers' certificate setting forth a copy of the resolution authorizing the capital contribution and the terms and conditions thereof shall be filed.

Comment. See the Comment to Section 5510.

This section is adapted from Section 401(a) of the General Corporation Law, a revision of former Section 1102. For definitions of "officers' certificate" and "filed," see Sections 5173 and 5169.

Article 3. Subventions

§ 5520. Subventions authorized

5520. The articles or bylaws may provide that a nonprofit corporation shall be authorized by resolution of the board to accept subventions from members or nonmembers on terms and conditions not inconsistent with this article, and to issue certificates therefor.

Comment. Sections 5520 through 5529 are new.

The sections in this article establish for California nonprofit corporations a new concept for long-term investment combining elements of equity and debt financing. The subvention device first appeared in Section 504 of New York's Not-for-Profit Corporation Law and later in Section 7541 of Pennsylvania's Corporation Not-for-profit Code. In exchange for issuing subventions, a nonprofit corporation may receive funds which are to be repaid only upon the occurrence of a specified event, such as the accomplishment of the purpose for which the funds were contributed or the lapse of a specified period of time, subject always to the prior rights of creditors and the financial health of the nonprofit corporation.

Section 5520 requires that a nonprofit corporation be authorized to accept subventions both by its articles and by board resolution. The resolution must be filed with an officers' certificate in the office of the Secretary of State (Section 5529).

§ 5521. Consideration

5521. A subvention may consist of such consideration as is determined from time to time by the board, or by the members if the articles or bylaws so provide, consisting of any or all of the following: money paid, labor done, services actually rendered to or for the benefit of or in the formation or reorganization of the nonprofit corporation, debts or securities canceled, and tangible or intangible property actually received by the nonprofit corporation. Neither promissory notes of a member nor obligations for future services shall constitute full or part payment of a subvention. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the nonprofit corporation shall be conclusive.

Comment. See the Comment to Section 5520.

Section 5511 is adapted from Section 409, defining valid consideration for the issuance of shares by a corporation, which is a revision of former Section 1109 (General Corporation Law).

§ 5522. Subordination

5522. The rights of holders of subvention certificates shall at all times be subordinate to the rights of creditors of the nonprofit corporation.

Comment. See the Comment to Section 5520.

§ 5523. Periodic payments

5523. The resolution of the board authorizing acceptance of the subventions may provide that the holders of the subvention certificates are entitled to a fixed or contingent periodic payment out of the assets of the nonprofit corporation equal to a percentage of the original amount or value of the subvention.

Comment. See the Comment to Section 5520.

Periodic payments to members pursuant to this section are subject to the requirements of Sections 5551 and 5552.

§ 5524. Redemption at option of nonprofit corporation

5524. The resolution of the board authorizing acceptance of the subventions may provide that subventions shall be redeemable, in whole or in part, at the option of the nonprofit corporation, at such price or prices (not to exceed the original amount or value of the subventions plus any periodic payments due or accrued thereon), within such period or periods, and on such terms and conditions, not inconsistent with this chapter, as are stated in the resolution.

Comment. See the Comment to Section 5520.

Comparable provisions in the General Corporation Law are Section 402(b) and former Section 1101.

Redemption payments to members pursuant to this section are subject to the requirements of Sections 5551 and 5552.

§ 5525. Redemption at option of holder

5525. The resolution of the board authorizing acceptance of the subventions may provide that holders of all or some subvention certificates shall have the right to require the nonprofit corporation after a specified period of time to redeem the certificates, in whole or in part, at a price or prices that do not exceed the original amount or value of the subventions plus any periodic payments due or accrued thereon, upon an affirmative showing that the financial condition of the nonprofit corporation will permit the required payment to be made without impairment of its operations or injury to its creditors. The right to require redemption may in addition be conditioned upon the occurrence of a specified event. For the purpose of enforcing their rights under this paragraph, holders of subvention certificates shall have the same right as an authorized member to inspect the books and records of the nonprofit corporation.

Comment. See the Comment to Section 5520.

Redemption of a subvention certificate at the option of its holder is consistent with the partial debt character of this device and with the concept of a subvention as a means of financing particular projects; this procedure is inconsistent with normal rules for redemption of equity interests. See Section 402 and former Section 1101 (General Corporation Law).

Payments to members pursuant to this section are subject to the requirements of Sections 5551 and 5552.

"Authorized member" is defined in Section 6620.

§ 5526. Payment upon dissolution

5526. Upon dissolution of the nonprofit corporation, holders of subvention certificates shall be entitled, after satisfaction of the claims of creditors, to a repayment of the original amount or value of the subvention plus any periodic payments due or accrued thereon unless a lesser sum is specified in the resolution of the board authorizing the acceptance of the subventions.

Comment. See the Comment to Section 5520.

This section establishes a general rule for repayment of subventions upon dissolution, subject to contrary provisions in the authorizing resolution of the board.

§ 5527. Transfer

5527. Subvention certificates shall be nontransferable unless the resolution of the board authorizing acceptance of the subventions provides that they are transferable, either at will or subject to specified restrictions.

Comment. See the Comment to Section 5520.

This section establishes the control of the nonprofit corporation over the transferability of subvention certificates, with nontransferable status in the absence of a specific resolution to the contrary.

§ 5528. Contents of certificate

5528. There shall appear upon the face of each subvention certificate the following information:

(a) That the issuer is a nonprofit corporation.

(b) That the certificate is transferable, either at will or subject to specified restrictions, if applicable.

(c) That the certificate is redeemable, if applicable.

(d) That periodic payment may be made thereon, if applicable.

Comment. See Comment to Section 5520.

For comparable provisions of the General Corporation Law, see Section 418(a) and former Sections 2401 and 2403.

§ 5529. Officers' certificate

5529. Before a nonprofit corporation issues a subvention certificate, an officers' certificate setting forth a copy of the resolution authorizing acceptance of the subventions and the terms and conditions thereof shall be filed.

Comment. See the Comment to Section 5520.

This section is adapted from Section 401(a) of the General Corporation Law, a continuation of former Section 1102.

For definitions of "officers' certificate" and "filed," see Sections 5173 and 5169.

Article 4. Debt§ 5530. Consideration

5530. A nonprofit corporation shall not issue bonds or other evidences of indebtedness except in exchange for consideration consisting of any or all of the following: money paid, labor done, services actually rendered to or for the benefit of or in the formation or reorganization of the nonprofit corporation, debts or securities canceled, and tangible or intangible property actually received by the nonprofit corporation. In the absence of fraud in the transaction, the judgment of the board as to the value of the consideration received by the nonprofit corporation shall be conclusive.

Comment. Sections 5530 and 5531 are new.

Former Section 9501(f) authorized nonprofit corporations to issue its notes, bonds, and other obligations. That general authority is continued in Section 5230. Sections 5530 and 5531 provide certain restrictions upon the issuance of debt instruments by nonprofit corporations which are derived from Section 506 of the New York Not-for-Profit Corporation Law and Section 7543 of the Pennsylvania Corporation Not-for-profit Code.

Section 5530 is adapted in part from Section 409(a) of the General Corporation Law, a revision of the provisions of former Section 1109.

§ 5531. Interest

5531. A nonprofit corporation may pay interest on its bonds or other evidences of indebtedness, may issue them at a discount, and may pay a premium for the redemption thereof prior to maturity, but the amount of such interest, discount, or premium received by holders thereof shall not be determined by or contingent upon the income or gain of the nonprofit corporation, nor shall such holders of bonds or other evidences of indebtedness receive at maturity more than the principal sum thereof plus interest due and accrued thereon.

Comment. See the Comment to Section 5530.

§ 5532. Payments to members

5532. A nonprofit corporation may repay the principal of, pay interest upon, issue at a discount, and pay a premium for the redemption prior to maturity of its bonds or other evidences of indebtedness held by members, subject to the provisions of Section 5531. No such payment of principal or interest, discount, or premium shall be deemed to be a distribution of gains, profits, or dividends.

Comment. Section 5532 is new. The general prohibition against distribution of gains, profits, or dividends to members is found in subdivision (a) of Section 5236. Section 5532 adds the payment upon evidences of indebtedness to members to the list of valid distributions set forth in subdivision (b) of Section 5236.

It should be noted that the restrictions of Sections 5551 and 5552 do not apply to such debt payments.

Article 5. Redemption§ 5540. Definition of certificate

5540. As used in this article, "certificate" shall mean any membership, capital, or subvention certificate.

Comment. Certificates which may be subject to redemption include membership certificates (Section 5405), capital contributions and certificates (Section 5510), and subvention certificates (Section 5520).

§ 5541. Method of redemption

5541. A nonprofit corporation may redeem any or all certificates which are redeemable at its option by (1) giving notice of redemption and (2) payment or deposit of the redemption price of the certificates as provided in its articles, bylaws, or board resolution authorizing issuance of the certificates, or deposit of the redemption price pursuant to Section 5544.

Comment. Sections 5541, 5542, 5543, and 5544 are adaptations of the provisions of Section 509 which continue the requirements for redemption of shares stated in former Sections 1700, 1701, 1702, and 1703 (General Corporation Law).

§ 5542. Notice of redemption

5542. (a) Subject to any provisions in the articles, bylaws, or the board resolution authorizing issuance of the certificates with respect to the notice required for redemption of certificates, a non-profit corporation may give notice of the redemption of any or all certificates subject to redemption by causing a notice of redemption to be published in a newspaper of general circulation in the proper county at least once a week for two successive weeks, in each instance on any day of the week, commencing not earlier than 60 nor later than 20 days before the date fixed for redemption.

(b) The notice of redemption shall set forth all of the following:

(1) The certificates to be redeemed.

(2) The date fixed for redemption.

(3) The redemption price.

(4) The place at which payment of the redemption price will be made upon surrender of the certificates.

Comment. See the Comment to Section 5541. "Proper county" is defined in Section 5177.

§ 5543. Mailing of notice

5543. If the nonprofit corporation gives notice of redemption pursuant to Section 5542, it shall also mail a copy of the notice of redemption to each holder of record of the certificates to be redeemed as

of the date of mailing or record date fixed in accordance with Section [701], addressed to the holder at the address of such holder appearing on the books of the nonprofit corporation or given by the holder to the nonprofit corporation for the purpose of notice or, if no such address appears or is given at the place where the principal executive office of the nonprofit corporation is located, not earlier than 60 nor later than 20 days before the date fixed for redemption. Failure to comply with this section does not invalidate the redemption of the certificates.

Comment. See the Comment to Section 5541.

Note. The proper section number relating to fixing a record date will be provided at a later date; that section will correspond to Section 701 of the General Corporation Law.

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§ 5544

§ 5544. Deposit of redemption price

5544. (a) If, on or prior to any date fixed for redemption of redeemable certificates, the nonprofit corporation deposits with any bank or trust company in this state as a trust fund a sum sufficient to redeem, on the date fixed for redemption thereof, the certificates called for redemption, with irrevocable instructions and authority to the bank or trust company to publish the notice of redemption thereof (or to complete such publication if theretofore commenced) and to pay, on and after the date fixed for redemption or prior thereto, the redemption price of the certificates to their respective holders upon the surrender

of their certificates, then from and after the date of the deposit (although prior to the date fixed for redemption) the certificates so called shall be redeemed and periodic payments on those certificates, if any, shall cease to accrue after the date fixed for redemption.

(b) The deposit shall constitute full payment for the certificates to their holders and, from and after the date of the deposit, the certificates shall no longer be outstanding and the holders thereof shall have no rights with respect thereto except the right to receive from the bank or trust company payment of the redemption price of the certificates without interest upon surrender of their certificates therefor.

Comment. See the Comment to Section 5541.

Article 6. Payments to Members

§ 5550. Payments to members

5550. Subject to the provisions of Section 5502 and this article, and to any further limitations in its articles or bylaws, a nonprofit corporation may make payments to members in order to purchase or redeem memberships, capital contributions, or subvention certificates.

Comment. Sections 5550 and 5551 are new.

Former Sections 1706 through 1708 (General Corporation Law) generally required the existence of earned surplus sufficient to make distributions. Section 500 now requires a corporation to have retained earnings or meet certain net worth and liquidity standards before making payments to shareholders. Sections 5550 and 5551 are adapted from Section 500.

Section 5550 provides for the purchase or redemption of memberships (Section 5262), capital contributions (Sections 5510-5515), and subvention certificates (Sections 5520-5528), thus enlarging the list of authorized distributions to members set forth in Section 5236(b).

§ 5551. Requirement for payments

5551. The payments provided in Section 5550 may be made only if either of the following requirements is met:

(a) The amount of the nonprofit corporation's fund balance of excess of revenues over expenditures immediately prior thereto equals or exceeds the amount of the proposed payment.

(b) Immediately after giving effect to the proposed payment:

(1) The sum of the assets of the nonprofit corporation (exclusive of goodwill, capitalized research and development expenses, and deferred charges) would be at least equal to 1-1/4 times its liabilities (not including deferred taxes, deferred income, and other deferred credits), and

(2) The current assets of the nonprofit corporation would be at least equal to its current liabilities or, if the average of the excess of revenues over expenses of the nonprofit corporation before taxes on income and before interest expense for the two preceding fiscal years was less than the average of the interest expense of the nonprofit corporation for such fiscal years, at least equal to 1-1/4 times its current liabilities. This paragraph is not applicable to a nonprofit corporation which does not classify its assets into current and fixed under generally accepted accounting principles.

(c) In determining the amount of the assets of the nonprofit corporation for the purposes of subdivision (b):

(1) No appreciation in value not yet realized shall in any event be included, except with respect to readily marketable securities, and profits derived from an exchange of assets shall not be included unless the assets received are currently realizable in cash.

(2) "Current assets" may include net amounts which the board has determined in good faith may reasonably be expected to be received during the 12-month period used in calculating current liabilities pursuant to existing contractual relationships obligating the parties to the contracts to make fixed or period payments during the term of the

contracts, or, in the case of public utilities, pursuant to service connections with customers, after in each case giving effect to future costs not then included in current liabilities but reasonably expected to be incurred by the nonprofit corporation in performing such contracts or providing service to utility customers.

(3) The amount of any payment in the form of property shall be determined on the basis of the value at which the property is carried on the nonprofit corporation's financial statements in accordance with generally accepted accounting principles.

Comment. See the Comment to Section 5550.

The specific standards contained in Section 5551 have been adapted from Section 500 to conform to generally accepted accounting principles for nonprofit corporations. These standards are augmented by the general solvency requirement of Section 5552.

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§ 5552

§ 5552. Payments to members prohibited

5552. A nonprofit corporation shall not make payments to members in order to purchase or redeem memberships, capital contributions, or subvention certificates as authorized by this chapter if the nonprofit corporation is, or as a result of such payment would be, likely to be unable to meet its liabilities (except those whose payment is otherwise adequately provided for) as they mature.

Comment. This section is adapted from Section 501 (General Corporation Law), which continues the substance of former Section 1708.

§ 5553. Effect of termination of membership

5553. Termination of membership in a nonprofit corporation, for any reason, shall be without prejudice to the terminated member's rights as a maker of a capital contribution, the holder of a subvention certificate, or the holder of a bond or other evidence of indebtedness.

Comment. Section 5553 is new. This section is adapted from Section 516 of New York's Not-for-Profit Corporation Law (1970).

This section distinguishes the property rights of a member in the nonprofit corporation from the rights he may have as a contributor of capital or holder of subvention certificates or evidences of indebtedness. The member's rights arising out of membership, financed by dues, assessments, and other charges, may cease upon membership termination (Section 5406), but his property rights (however limited) generated by the financing devices authorized by Articles 2, 3, and 4 of this chapter continue.

§ 5554. Payment upon termination of membership

5554. Unless otherwise provided in the resolution of the board authorizing the capital contribution, a nonprofit corporation may at its option in the event of a termination of membership redeem any capital contribution or certificate of the former member upon payment of a sum of money equal to the redemption price thereof if such contribution or certificate is by its terms redeemable, or upon the payment of a sum of money equal to the amount of the capital contribution if it is not by its express terms redeemable.

Comment. Section 5554 is new. It is adapted from Section 516 of New York's Not-for-Profit Corporation Law (1970).

Payments made pursuant to this section remain subject to the requirements of Sections 5551 and 5552.

Article 7. Trust Property

§ 5560. Management of charitable property

5560. (a) This section is applicable to all property received by a nonprofit corporation for charitable purposes and to all property, unless the donor or instrument transferring the property provides otherwise, received by a nonprofit corporation which is organized for charitable purposes.

(b) In acquiring, purchasing, investing, reinvesting, exchanging, selling, and otherwise managing property described in subdivision (a), a nonprofit corporation and its directors shall be subject to the obligations of a trustee set forth in Section 2261 of the Civil Code.

Comment. Section 5560 is new.

This section states existing case law that the management duty of the corporation holding charitable assets is that of the private trustee. Lynch v. John M. Redfield Foundation, 9 Cal. App.3d 293, 298 (1970). Whether a corporation is organized for charitable purposes is a fact question determined by reference to both its articles and the manner of conducting its activities. See Lynch v. Spilman, 67 Cal.2d 251 (1967).

Section 2261 of the Civil Code requires a trustee to exercise the judgment of a "prudent investor," subject to the specific directions of any document creating the trust and to the orders of an appropriate court. The obligations of a trustee are in addition to those imposed upon directors by Section 5370.

§ 5561. Indefinite purposes

5561. No bequest, devise, gift, or transfer of property to a non-profit corporation for a charitable purpose is invalid because of indefiniteness or uncertainty as to the purposes or the beneficiaries thereof, but, to the extent to which such indefiniteness or uncertainty exists, it shall be resolved by the nonprofit corporation in the manner which, in its judgment, is most consonant with the purpose of the donor and most conducive to the public welfare.

Comment. Section 5561 continues the substance of a portion of former Section 10206(b).

This section establishes the principle that charitable gifts shall not fail because of uncertainty as to the donor's intentions and the rule that a nonprofit corporation has the authority to resolve any such ambiguities. Charitable purposes are not defined by statute but are left to judicial development.

§ 5562. Institutional trustee

5562. (a) Any nonprofit corporation may transfer, by appropriate action of its board, any or all of its assets, including property held upon a charitable trust, to an institutional trustee, which shall be an entity entitled under Section 1500 of the Financial Code to engage in the trust business as, trustee and with like investment restrictions.

(b) Upon such transfer, the board shall be relieved of all liability for the administration of such assets for as long as the assets are

administered by the institutional trustee.

(c) The institutional trustee shall pay, at least semiannually, the net income from the transferred assets, which may include so much of the realized appreciation of principal as the board determines to be prudent, to the nonprofit corporation for use and application to the purpose or purposes for which the assets were received by the corporation.

Comment. Section 5562 is new.

This section continues and expands the authority given to charitable corporations by former Section 10204 to delegate management of investments. See also Civil Code § 2290.5. It is derived from and similar in substance to provisions of the nonprofit corporation laws of Pennsylvania and New York. Pa. Stat. Ann. tit. 15, § 7551 (1972); N.Y. Not-for-Profit Corp. Law § 514 (McKinney 1970).

Subdivision (a) limits the choice of institutional trustee to an entity qualified under Section 1500 of the Financial Code, which involves approval of the Superintendent of Banks, certain capital and surplus requirements, and a required deposit with the State Treasurer.

Subdivision (b) exempts the directors from all further liability for mismanagement of such transferred assets. This protection does not relieve the directors from their duty to exercise due care in the selection of the institutional trustee and in the continuation or termination of the trust. See Sections \_\_\_\_, 1560).

Subdivision (c) requires the institutional trustee to pay over income periodically to the nonprofit corporation, which is consistent with general policy against excessive accumulation of income in charitable trusts.

§ 5563. Private foundations

5563. (a) This section applies to a nonprofit corporation during any period or periods the nonprofit corporation is deemed to be a "private foundation" as defined in Section 509 of the Internal Revenue Code of 1954, and any provision contained in its articles or other governing instrument inconsistent with this section or to the contrary thereof shall be without effect.

(b) A nonprofit corporation described in subdivision (a) shall distribute its income (and principal, if necessary) for each taxable year at such time and in such manner as not to subject it to tax under Section 4942 of the Internal Revenue Code of 1954.

(c) A nonprofit corporation described in subdivision (a) shall not do any of the following:

(1) Engage in any act of self-dealing as defined in subdivision (d) of Section 4941 of the Internal Revenue Code of 1954.

(2) Retain any excess business holdings as defined in subdivision (c) of Section 4943 of the Internal Revenue Code of 1954.

(3) Make any investments in such manner as to subject it to tax under Section 4944 of the Internal Revenue Code of 1954.

(4) Make any taxable expenditure as defined in subdivision (d) of Section 4945 of the Internal Revenue Code of 1954.

Comment. Section 5564 is the same in substance as former Section 9501.1.

§ 5564. Attorney General supervision

5564. (a) A nonprofit corporation which holds property subject to any charitable trust is subject at all times to examination by the Attorney General, on behalf of the state, to ascertain the condition of its affairs and to what extent, if at all, it may fail to comply with trusts which it has assumed or may depart from the general purposes for which it is formed.

(b) In case of any such failure or departure, the Attorney General shall institute, in the name of the state, the proceedings necessary to correct the noncompliance or departure.

Comment. Section 5564 continues the substance of former Section 9505. Cf. former Section 10207 (supervision of charitable corporations).

The Attorney General has inherent power at common law to superintend the management of all charities. People v. Cogswell, 113 Cal. 129, 136 (1896). Additional procedures for supervision by the Attorney General are available under the Uniform Supervision of Trustees for Charitable Purposes Act (Govt. Code §§ 12580-12597).

Interested individuals other than the Attorney General may also have standing to compel proper utilization of charitable property held by a nonprofit corporation. See Section 5232; Holt v. College of Osteopathic Physicians & Surgeons, 61 Cal.2d 750 (1964); San Diego etc. Boy Scouts of America v. City of Escondido, 14 Cal. App.3d 189 (1971); In re Veterans' Industries, Inc., 8 Cal. App.3d 902 (1970).

Article 3. Common Trust Fund§ 5570. Establishment

5570. If authorized to do so by its articles or bylaws, a nonprofit corporation organized for charitable purposes may establish one or more common trust funds for the purpose of furnishing investments to such corporation and to any other nonprofit corporation or organization organized for charitable purposes affiliated with it or to any organization, society, or corporation holding funds or property for the benefit of any of the foregoing, whether holding such funds or property as fiduciary or otherwise.

Comment. Section 5570 continues in substance a portion of former Section 10250(a), authorizing a nonprofit corporation with charitable purposes to create one or more common trust funds. The former definition of organizations which may also invest in the fund has been simplified to include any affiliated organization with charitable purposes and any organizations holding funds for such entities.

§ 5571. Investment

5571. Notwithstanding the provisions of any general or special law in any way limiting the right of any corporation, organization, or society, described in Section 5570, or the directors thereof, as fiduciary or otherwise, to invest funds held by them, it shall be lawful for any such corporation, organization, or society, or the directors there-

of, to invest any or all of their funds or property in shares or interests of common trust funds established pursuant to this article; provided that, in the case of funds or property held as fiduciary, such investment is not prohibited by the wording of the will, deed, or other instrument creating such fiduciary relationship.

Comment. Section 5571 continues the provisions of a portion of former Section 10250(a).

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§ 5572

§ 5572. Administration

5572. The directors or trustees of any common trust fund, organized pursuant to this article, may do all of the following:

(a) Employ such officers or agents as they think best, define their duties, and fix their compensation.

(b) Appoint as custodian of the trust estate an entity entitled under Section 1500 of the Financial Code to engage in the trust business.

(c) Employ an investment adviser or advisers, define their duties, and fix their compensation.

(d) Deposit securities which constitute part or all of the trust estate in a securities depository, as defined in Section 30004 of the Financial Code, which is licensed under Section 30200 of the Financial Code or exempted from licensing thereunder by Section 30005 or 30006 of the Financial Code. The securities may be held by the securities depository in the manner authorized by Section 775 of the Financial Code.

Comment. Section 5573 is the same in substance as former Section 10250(b). General authority to convey charitable assets to an institutional trustee is contained in Section 5563.

405/778

§ 5573

§ 5573. Dividends

5573. The directors or trustees of any common trust fund established pursuant to this article shall pay ratably among the holders of shares or beneficial certificates then outstanding, semiannual dividends which shall approximately equal, in each fiscal year, the net income of the trust.

Comment. This section is substantially the same as former Section 10250(c).

405/781

§ 5574

§ 5574. Educational institution

5574. "Educational institution," as used in this article, means both:

(a) A nonprofit corporation organized under the provisions of Chapter 1 (commencing with Section 29001), the Education Code, or under this division for the purpose of establishing, conducting, or maintaining an

institution offering courses beyond high school and issuing or conferring a diploma or for the purpose of offering or conducting private school instruction on the high school or elementary school level and any charitable trust organized for such purpose or purposes.

(b) The University of California, the state colleges, the state community colleges, and any auxiliary organization, as defined in Section 24054.5 of the Education Code, established for the purpose of receiving gifts, property, and funds to be used for the benefit of a state college.

Comment. Section 5574 is the same in substance as former Section 10251(a).

405/786

§ 5575

§ 5575. Membership in nonprofit corporation for maintenance of common trust fund

5575. It shall be lawful for any educational institution to become a member of a nonprofit corporation incorporated under the laws of any state for the purpose of maintaining a common trust fund or similar common fund in which nonprofit organizations may commingle their funds and property for investment and to invest any and all of its funds, whenever and however acquired, in such common fund or funds; provided, that, in the case of funds or property held as fiduciary, such investment is not prohibited by the wording of the will, deed or other instrument creating such fiduciary relationship.

Comment. Section 5575 is the same as former Section 10251(b).

§ 5576. Distributions to educational institution

5576. An educational institution electing to invest in a common fund or funds under the provisions of this article may do the following:

(a) Elect to receive distributions from each such fund in an amount not to exceed for each fiscal year the greater of the income, as defined in Section 730.03 of the Civil Code, accrued on its interest in such fund or 10 percent of the value of its interest in such fund as of the last day of its next preceding fiscal year.

(b) Expend such distribution or distributions for any lawful purpose notwithstanding the provisions of any general or special law characterizing such distribution, or any part thereof, as principal or income; provided, that, in the case of funds or property invested as fiduciary, such expenditure is not prohibited by the wording of the will, deed, or other instrument creating such fiduciary relationship. No such prohibition of expenditure shall be deemed to exist solely because a will, deed, or other such instrument, whether executed or in effect before or after the effective date of this section, directs or authorizes the use of only the "income," or "interest," or "dividends," or "rents, issues, or profits," or contains words of similar import.

Comment. Section 5576 is the same in substance as former Section 10251(c).

§ 5577. Application of Corporate Securities Law

5577. The provisions of the Corporate Securities Law do not apply to the creation, administration, or termination of common trust funds created under this article, or to participation therein.

Comment. Section 5577 is the same in substance as former Sections 10250(d) and 10251(d).

Tentatively Approved  
February 1976

APPENDIX

Corporations Code § 9301 (repealed)

9301. The authorized number and qualifications of members of the corporation, the different classes of membership, if any, the property, voting, and other rights and privileges of members, and their liability to dues or assessments and the method of collection thereof, shall be set forth either in the articles or in the by-laws, which shall not, however, provide for the issuance of more than one membership to any member.

If the voting, property or other rights or interests, or any of them, be unequal, the articles or by-laws shall set forth the rule or rules by which the respective voting, property or other rights or interests of each member or class of members are fixed and determined.

The articles or by-laws may authorize dues or assessments or both to be levied upon all members or classes of membership alike, or in different amounts or proportions or upon a different basis upon different members or classes of membership and may exempt some members or classes of membership from either dues or assessments, or both.

The articles or by-laws may fix the amount and method of collection of dues or assessments or both, or may authorize the board of directors to fix the amount thereof from time to time, and make them payable at such times or intervals, and upon such notice, and by such methods as the directors may prescribe. Dues or assessments or both may be made enforceable by action or by the sale or forfeiture of membership, or both, upon reasonable notice.

Comment. The first two sentences of former Section 9301 are continued in Section 5261 with the exception of the proviso relating to more than one membership, which is superseded by Section 5400. The third and fourth sentences are continued in Section 5500.

045/185

Corp. Code § 9501.1

Corporations Code § 9501.1 (repealed)

9501.1. Every nonprofit corporation, during any period or periods such corporation is deemed to be a "private foundation" as defined in Section 509 of the Internal Revenue Code of 1954 as amended by Section 101 of the Tax Reform Act of 1969 (all references in this section to the Internal Revenue Code shall refer to such code as amended by such act), shall distribute its income for each taxable year (and principal, if necessary) at such time and in such manner as not to subject such corporation to tax under Section 4942 of such code (as modified by paragraph (3) of subsection (1) of Section 101 of the Tax Reform Act of 1969), and such corporation shall not engage in any act of self-dealing as defined in subsection (d) of Section 4941 of such code (as modified by paragraph (2) of subsection (1) of Section 101 of the Tax Reform Act of 1969), retain any excess business holdings as defined in subsection (c) of Section 4943 of such code, make any investments in such manner as to subject such corporation to tax under Section 4944 of such code, or make any taxable expenditure as defined in subsection (d) of Section

4945 of such code (as modified by paragraph (5) of subsection (1) of Section 101 of the Tax Reform Act of 1969).

This section shall apply to any such corporation and any provision contained in its articles of incorporation or other governing instrument inconsistent with this section or to the contrary thereof shall be without effect.

Comment. Former Section 9501,1 is continued in Section 5563.

045/186

Corp. Code § 9505

Corporations Code § 9505 (repealed)

9505. A nonprofit corporation which holds property subject to any public or charitable trust is subject at all times to examination by the Attorney General, on behalf of the State, to ascertain the condition of its affairs and to what extent, if at all, it may fail to comply with trusts which it has assumed or may depart from the general purposes for which it is formed. In case of any such failure or departure the Attorney General shall institute, in the name of the State, the proceedings necessary to correct the noncompliance or departure.

Comment. Former Section 9505 is continued in Section 5564.

Corporations Code § 10250 (repealed)

10250. (a) Any corporation organized under the provisions of or for the purposes set forth in Part 2 (commencing with Section 10000) or Part 3 (commencing with Section 10200) of this division may, if authorized so to do by its articles of incorporation, establish one or more common trust funds for the purpose of furnishing investments to such corporation or to any church, parish, congregation, society, chapel, mission, religious, beneficial, charitable or educational institution affiliated with it, or to any organization, society or corporation holding funds or property for the benefit of any of the foregoing, or holding funds for the purpose of supporting a bishop, priest, religious pastor, or teacher or any building or buildings used by or owned by any of the foregoing, whether holding such funds or property as fiduciary or otherwise. Notwithstanding the provisions of any general or special law in any way limiting the right of any of the foregoing or the officers or directors thereof, as fiduciary or otherwise, to invest funds held by them, it shall be lawful for any of the foregoing to invest any or all of their funds or property in shares or interests of such common trust fund or trust funds; provided, that, in the case of funds or property held as fiduciary, such investment is not prohibited by the wording of the will, deed or other instrument creating such fiduciary relationship.

(b) The directors or trustees of any such common trust fund, or trust funds, so organized, may employ such officers or agents as they think best, define their duties, and fix their compensation. They may also appoint a trust company or bank as custodian of the trust estate and may employ an investment adviser or advisers, define their duties,

and fix their compensation. Securities which constitute part or all of the trust estate may be deposited in a securities depository, as defined in Section 30004 of the Financial Code, which is licensed under Section 30200 of the Financial Code or exempted from licensing thereunder by Section 30005 or 30006 of the Financial Code, and such securities may be held by such securities depository in the manner authorized by Section 775 of the Financial Code.

(c) The directors or trustees of any such common trust fund, or trust funds, shall pay ratably among the holders of shares or beneficial certificates then outstanding, semiannual dividends which shall approximately equal, in each fiscal year, the net income of the trust, or trusts.

(d) The provisions of the Corporate Securities Law shall not apply to the creation, administration, or termination of common trust funds created hereunder, nor to participation therein.

Comment. The first sentence of subdivision (a) of former Section 10250 is continued in Section 5570. The second sentence is continued in Section 5571. Subdivision (b) is continued in Section 5572. Subdivision (c) is continued in Section 5573. Subdivision (d) is continued in Section 5577.

Corporations Code § 10251 (repealed)

10251. (a) "Educational institution," as used in this section, means any nonprofit corporation organized under the provisions of Chapter 1 (commencing with Section 29001), Division 21, of the Education Code or under the provisions of Part 1 (commencing with Section 9000) or Part 3 (commencing with Section 10200) of this division for the purpose of establishing, conducting or maintaining an institution offering courses beyond high school and issuing or conferring a diploma or for the purpose of offering or conducting private school instruction on the high school or elementary school level and any charitable trust organized for such purpose or purposes. "Educational institution," as used in this section, also means the University of California, the state colleges, the state community colleges and any auxiliary organization, as defined in Section 24054.5 of the Education Code, established for the purpose of receiving gifts, property and funds to be used for the benefit of a state college.

(b) It shall be lawful for any educational institution to become a member of a nonprofit corporation incorporated under the laws of any state for the purpose of maintaining a common trust fund or similar common fund in which nonprofit organizations may commingle their funds and property for investment and to invest any and all of its funds, whenever and however acquired, in such common fund or funds; provided, that, in the case of funds or property held as fiduciary, such investment is not prohibited by the wording of the will, deed or other instrument creating such fiduciary relationship.

(c) An educational institution electing to invest in a common fund or funds under the provisions of this section may elect to receive distributions from each such fund in an amount not to exceed for each fiscal year the greater of the income, as defined in Section 730.03 of the Civil Code, accrued on its interest in such fund or 10 percent of the value of its interest in such fund as of the last day of its next preceding fiscal year. The educational institution may expend such distribution or distributions for any lawful purpose notwithstanding the provisions of any general or special law characterizing such distribution, or any part thereof, as principal or income; provided, that, in the case of funds or property invested as fiduciary, such expenditure is not prohibited by the wording of the will, deed or other instrument creating such fiduciary relationship. No such prohibition of expenditure shall be deemed to exist solely because a will, deed or other such instrument, whether executed or in effect before or after the effective date of this section, directs or authorizes the use of only the "income," or "interest," or "dividends" or "rents, issues or profits," or contains words of similar import.

(d) The provisions of the Corporate Securities Law of 1968 shall not apply to the creation, administration or termination of common trust funds authorized under this section, or to participation therein.

Comment. Subdivision (a) of former Section 10251 is continued in Section 5574. Subdivision (b) is continued in Section 5575. Subdivision (c) is continued in Section 5576. Subdivision (d) is continued in Section 5577.